Supreme Court U.S.
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No. 02-857

IN THE

Supreme Court of the United States

OCTOBER TERM, 2002

HOUSEHOLD CREDIT SERVICES, INC.
and MBNA AMERICA BANK, N.A.,

Petitioners,

—v.—

SHARON R. PFENNIG,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITIONERS' REPLY BRIEF

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February 12, 2003

List of Parties and Rule 29.6 Statement

There have been no changes in the information previously submitted by petitioners pursuant to Rule 29.6 in their petition for a writ of certiorari.

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PETITIONERS' REPLY BRIEF

Respondent does not dispute that the Sixth Circuit invalidated a provision of Regulation Z, the regulations issued by the Federal Reserve to implement TILA. That the court held a federal regulation—unchallenged for over two decades—invalid is itself grounds for certiorari, quite apart from the severe practical consequences of the decision for the banking industry. At a minimum, the Court should call for the views of the Solicitor General to permit a further presentation of the Federal Reserve's views on the issue. (*See also* Pet. App. at A43-53.)

1. The question presented is undeniably important. Contrary to respondent's assertion (Opp'n at 3), the petition does not ask the Court simply to correct an erroneous legal ruling of concern only to the parties. The American Bankers Association, Consumer Bankers Association, American Financial Services Association, MasterCard International Incorporated and Visa U.S.A. Inc.—entities that speak for the entire banking industry—have submitted a brief in support of the petition emphasizing that the question presented "is of substantial importance to the banking industry as a whole

and will have severe consequences if not reversed." (Industry *Amici* Br. at 3.) As those *amici* explain (*id.* at 2-3, 12-16), the decision below, if allowed to stand, will create enormous compliance problems for and impose substantial financial costs on the banking industry, a view also expressed by the Federal Reserve in its *amicus* brief in the Sixth Circuit. (Pet. App. at A43, A51-52.)

Respondent's effort to minimize the practical implications of the decision does not withstand scrutiny. Both Chief Judge Edgar in his dissent and the Federal Reserve in its *amicus* brief observed that the decision below establishes a new and different disclosure rule in the Sixth Circuit, whereas Regulation Z continues to apply in other circuits. (Pet. App. at A22-23, A51-52.) Respondent dismisses this concern, stating that "Petitioners fail to identify how requiring credit card issuers to comply with the plain language of TILA creates differing obligations from circuit to circuit." (Opp'n at 6.) As the Federal Reserve stated, however, the Sixth Circuit's decision does not relieve credit card issuers of their obligation to comply with Regulation Z in other circuits. (Pet. App. at A51.) Because the obligations imposed by the Sixth Circuit's decision and Regulation Z are diametric opposites, creditors cannot implement a single nationwide disclosure that complies with both.

2. The Sixth Circuit's decision creates a conflict in the law governing creditors' disclosure obligations nationwide. In opposing certiorari, respondent relies principally on the absence of a strict circuit split on the precise question presented. (Opp'n at 1-2.) Although no other court of appeals has addressed the validity of Regulation Z's exclusion of over-limit fees from the finance charge, review by this Court is still necessary to bring about uniformity in the law among the circuits. As noted above, absent a decision by this Court, credit card issuers will have to comply with Regulation Z outside the Sixth Circuit and with a separate and conflicting rule within the Sixth Circuit. As a result, "regardless of

whether there is a split in judicial decisions concerning the validity of [12 C.F.R.] § 226.4(c)(2), nationwide creditors are subjected to conflicting legal obligations." (Industry *Amici* Br. at 13.)

3. The Sixth Circuit failed to accord the proper deference to the Federal Reserve's reasonable interpretation of TILA. The statute does not unambiguously provide that over-limit fees are part of the finance charge. It is silent on that precise question. Accordingly, the Federal Reserve issued a regulation that implements TILA's general language and provides specific guidance to creditors. That regulation excludes charges such as over-limit fees, late fees and other default fees from the finance charge on the ground that they are imposed not as "an incident to the extension of credit," but rather as an incident to a consumer's violation of the credit agreement. (Pet. App. at A45-51.) The Federal Reserve's interpretation of TILA reflected in that regulation is not "demonstrably irrational." *Ford Motor Co.* v. *Milhollin*, 444 U.S. 555, 565 (1980). Even the Sixth Circuit agreed that the Federal Reserve properly excluded late fees and other default fees from the finance charge because such fees are imposed as a result of the consumer's violation of the credit agreement. (Pet. App. at A13-14.)

Respondent argues that the Sixth Circuit "acknowledged" that the Federal Reserve's interpretation of TILA is entitled to deference. (Opp'n at 2.) Although it recited the proper standard, the Sixth Circuit did not faithfully apply it, rejecting the Federal Reserve's interpretation of the statute and substituting instead what the court believed to be "a liberal interpretation in favor of consumers." (Pet. App. at A8.) Rather than interpret TILA's general language itself—liberally or otherwise—the Sixth Circuit was required under *Milhollin* to defer to the Federal Reserve's rational interpretation of the statute.

4. The Sixth Circuit also exceeded its judicial role in attempting to determine on its own which rule would best

"protect [consumers] in credit transactions." (Pet. App. at A8-9.) Based on its broad experience and expert judgment, the Federal Reserve concluded that consumers are better able to compare the costs of credit if over-limit fees are separately disclosed as "other charges" and not included in the finance charge. That determination is based on a reasonable interpretation of TILA, and it is well within the Federal Reserve's broad authority to make such "classifications" as in its judgment are necessary to effectuate the purposes of the statute. 15 U.S.C. § 1604(a). As this Court observed in *Milhollin*, "a court that tries to chart a true course to the Act's purpose embarks upon a voyage without a compass when it disregards the agency's views." 444 U.S. at 568.

5. In arguing that the fee in this case was imposed "incident to the extension of credit," respondent contends that petitioners authorized her to incur the charge that put her over her credit limit. (Opp'n at 5, 7.) That contention is found nowhere in respondent's complaint, and thus cannot properly be considered on a motion to dismiss. (*See* Pet. App. at A21.) More fundamentally, the merchant authorization system on which respondent relies is *not* a means by which creditors authorize cardholders at the time of a transaction to exceed their credit limits. (*See id.* at A48-51; Industry *Amici* Br. at 6-10.) It is thus not at all accurate to say, as the Sixth Circuit did, that petitioners "renegotiate[d] the agreement" with respondent. (Pet. App. at A13.) There was no communication between petitioners and respondent concerning the credit limit applicable to respondent's account.

Contrary to respondent's suggestion (Opp'n at 5), petitioners have never conceded that the fee in this case was imposed "incident to the extension of credit." Instead, petitioners have always argued, as they do here, that the statute does not address the precise question at issue and that therefore *Milhollin* requires courts to defer to the Federal Reserve's rational interpretation of the statute. *See* Brief of

Defendants-Appellees at 11, 14, *Pfennig* v. *Household Credit Servs., Inc.*, 295 F.3d 522 (6th Cir. 2002) (No. 00-4213).

6. The fee at issue in this case was a legitimate over-limit fee. Respondent accuses petitioners of "attempting to avoid disclosure of a true finance charge by calling it an 'over-limit fee,' so as to hide behind the protection of the Federal Reserve Board's regulation." (Opp'n at 7.) This contention cannot even be reconciled with the Sixth Circuit's decision. The Sixth Circuit stated that "it is undisputed that the fee at issue in this case was imposed for 'exceeding a credit limit.'" (Pet. App. at A17.) The court thus held that petitioners are entitled to immunity from damages under 15 U.S.C. § 1640(f) because they complied in good faith with Regulation Z. (*Id.* at A18 n.6.) In short, respondent's suggestion (Opp'n at 6) that "over-limit fee" was simply a "label" that petitioners "arbitrarily assigned" to the fee in this case is false.

* * *

The petition should be granted. At a minimum, the Court should call for the views of the Solicitor General.

Respectfully submitted,

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